

Internal Revenue Service

Appeals Office
San Jose Appeals, MS-7100
55 S. Market St., Suite 440
San Jose, CA 95113

Release Number: **201525014**

Release Date: 6/19/2015

Date: March 24, 2015

Department of the Treasury

Employer Identification Number:

Person to Contact:

Employee ID Number:

Tel:

Fax:

Contact Hours:

UIL:

7871 .01-00

Certified Mail

Dear

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (the "Code"). It is determined that you do not qualify as exempt from Federal income tax under section 501(c)(3) of the Code.

Our adverse determination] was made for the following reason(s):

- You do not meet the organizational test because your Certificate of Incorporation does not limit your purpose to the exempt purposes in accordance with section 1.501(c)(3)-1(b)(1)(i) and does not dedicate your assets to the exempt purpose upon dissolution in accordance with section 1.501(c)(3)-1(b)(4), respectively, of the Federal income tax regulations.
- You do not meet the operational test because:
 - (a) Your loan program is not limited to a charitable class of people, as your only requirement is that the farmer has a farm or farms located in the United States or the United States territories.
 - (b) There is no established procedure including record keeping in place to ensure that the loan money will be used by the recipients for intended exempt purposes only.
 - (c) You were formed based on the intellectual property of the founder but you do not reveal any arrangement made with the founder regarding to the use of his intellectual property.
 - (d) You plan to rely solely on public support, yet you will be operated by one person, who will determine his own salary without further explanation as to how reasonable compensation is set and how the amount will be related to his actual work performance.
 - (e) You do not have a community-based board and do not have conflict of interest policy in place to safeguard charitable assets from being diverted for any private purposes.

Contributions to your organization are not deductible under section 170 of the Code.

You are required to file Federal income tax returns on Forms 1120. File your return with the appropriate Internal Revenue Service Center per the instructions of the return. For further instructions, forms, and information please visit www.irs.gov.

If you were a private foundation as of the effective date of the adverse determination, you are considered to be taxable private foundation until you terminate your private foundation status under section 507 of the Code. In addition to your income tax return, you must also continue to file Form 990-PF by the 15th Day of the fifth month after the end of your annual accounting period.

Processing of income tax returns and assessments of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Code.

We will make this letter and the proposed adverse determination letter available for public inspection under Code section 6110 after deleting certain identifying information. We have provided to you, in a separate mailing, Notice 437, *Notice of Intention to Disclose*. Please review the Notice 437 and the documents attached that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437.

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of section 7428 of the Code in one of the following three venues: 1) United States Tax Court, 2) the United States Court of Federal Claims, or 3) the United States District Court for the District of Columbia. A petition or complaint in one of these three courts must be filed within 90 days from the date this determination letter was mailed to you. Please contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217. See also Publication 892.

You also have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States Court. The Taxpayer Advocate can however, see that a tax matters that may not have been resolved through normal channels get prompt and proper handling. If you want Taxpayer Advocate assistance, please contact the Taxpayer Advocate for the IRS office that issued this letter. You may call toll-free, 1-877-777-4778, for the Taxpayer Advocate or visit www.irs.gov/advocate for more information.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely Yours,

Appeals Team Manager

Enclosure: Publication 892 and/or 556



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: **FEB 27 2014**

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

B =

M =

X =

Dear

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code (I.R.C.) § 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under § 501(c)(3). The basis for our conclusion is set forth below.

Facts:

You are a not-for-profit corporation seeking recognition of exemption under § 501(c)(3). You did not indicate under which section of § 509(a) you seek foundation classification.

According to your Certificate of Incorporation ("Certificate"), you are a non-stock corporation formed for the purpose of providing struggling farmers with financial arrangements enabling them to avoid foreclosure after they've exhausted other means of assistance. You have one director, B, who will also serve as your sole employee and sole officer.

Your Statement of Purpose states that you will advertise to solicit funds from the general public, and that you will also solicit grants. Any participating farmer would have three options. The first option is a zero-interest loan to be paid back eventually. The second option is that you will buy an interest in the farm from the farmer, with the right to purchase the interest in the farm back from you. The third option is that you will purchase the entire farm from the farmer, the farmer is retained as manager of the farm, and the farmer retains the right to purchase the farm back from you.

You state that your program is designed to help poor and/or distressed farmers. All farmers with farms in the U.S. or U.S. territories are eligible for your loans. Your loan application

requests the name, address, phone, social security number, and driver's license number of the applicant. The applicant must submit income tax returns, property tax bills, mortgage statements, and any documentation related to the farmer's debt or liens against property. The applicant must sign a statement promising to pay back to you the amount loaned to the applicant by you, in full, without interest. B will determine how much, if any, the farmer will receive in loans. You have no other selection criteria.

You will not make additional loans to those recipients that admit that the loan funds they received were not used for the purposes he or she previously disclosed to you. You will attempt any legal means to recoup such outstanding loan amounts.

If you purchase a portion of or the entire interest in a participating farmer's property, B will determine the purchase amount based on the assessed value of the property and improvements. In the event that you purchase an entire interest and the farmer is retained as manager, the farmer manager will be charged with all decisions regarding the property, other than the decision to sell the property to a third party. If such a farm is sold to a third party, any sale proceeds in excess of the sum of the purchase amount you paid to the participating farmer and additional amounts loaned to the farmer will be returned to the farmer.

You state that any donations received from the public will be added to the revolving loan fund and available to farmers. You state 80% of the grants will be lent to farmers, and that 20% of the grants will go to your administration.

You do not have a conflict of interest policy. B's salary will be capped at \$x annually, and you state this amount is fair as compared to the salaries paid to executives at large non-profits. B has written, copyrighted, and owns M from which the structure of your operations is designed. You have not yet begun operations and have had no revenue.

LAW

I.R.C. § 501(c)(3) provides an exemption for corporations organized and operated exclusively for religious, charitable, scientific literacy, or educational purposes, no part of the net earnings of which inures to the benefit of any shareholder or individual.

Treas. Reg. § 1.501(c)(3)-1(a)(1) states that to be described in § 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Treas. Reg. § 1.501(c)(3)-1(b)(1)(i) states that an organization is organized exclusively for one or more exempt purposes only if its articles of organization limit the purposes of the organization to one or more exempt purposes and do not expressly empower the organization to engage, other than as an insubstantial part of its activities, in activities which are not in furtherance of one or more exempt purposes.

Treas. Reg. § 1.501(c)(3)-1(b)(4) provides that an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose.

Treas. Reg. § 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in § 501(c)(3). An organization will

not be regarded as exempt if more than an insubstantial part of its activities further a non-exempt purpose.

Treas. Reg. § 1.501(c)(3)-1(d)(1) provides that an organization may be recognized as exempt under § 501(c)(3) if it is operated exclusively for one or more of the following purposes: religious, charitable, scientific, testing for public safety, literary, educational, or prevention of cruelty to children or animals.

Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. To meet the requirements of this subsection, an organization must establish that it is not organized or operated for the benefit of private interests, such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Treas. Reg. § 1.501(c)(3)-1(d)(2) expressly provides that relief of the poor, or distressed, or underprivileged is a charitable purpose.

Rev. Rul. 56-304, 1956-2 C.B. 306, states that a § 501(c)(3) organization can make a distribution to an individual, provided such distribution is made on a true charitable basis in furtherance of the organization's charitable purposes. However, such organizations should maintain adequate records and case histories to show the name and address of each recipient of aid; the amount distributed to each; the purpose for which the aid was given; the manner in which the recipient was selected and the relationship, if any, between the recipient and (1) members, officers, or trustees of the organization, (2) a grantor or substantial contributor to the organization or a member of the family of either, in order that any or all distributions made to individuals can be substantiated upon request by the Internal Revenue Service.

Rev. Rul. 70-186, 1970-1 C.B. 129, described a nonprofit organization formed and operated in preserving and improving a lake for public recreation. The organization was financed by contributions from lake front property owners, from members of the community adjacent to the lake, and from municipalities bordering the lake. Because the organization insured the continued use of the lake for public recreational purposes, it was performing a charitable activity. The benefits derived from the organization's activities flowed principally to the general public through the maintenance and improvement of public recreational facilities, and that any private benefits derived by the lake front property owners did not lessen the public benefits flowing from the organization's operations. In fact, it would have been impossible for the organization to accomplish its purposes without providing benefits to the lake front owners. Thus, the Service ruled that the organization was exempt under § 501(c)(3).

Rev. Rul. 74-587, 1974-2 C.B. 162, holds that a nonprofit organization that provides financial assistance to businesses otherwise unable to obtain funds from conventional commercial sources due to their location in depressed urban communities or the proprietor's membership in a minority or other disadvantaged group qualified for exemption. The organization activities furthered the exempt purposes of relieving poverty, eliminating prejudice, reducing neighborhood tensions, and combating community deterioration.

Rev. Rul. 76-419, 1976-2 C.B. 146, provides an organization that induced industrial enterprises to locate in an economically depressed area and to hire and train the underemployed and unemployed in that area is exempt. The organization's activities serve not only to relieve poverty, but also to lessen neighborhood tensions caused by the lack of jobs and job

opportunities in the area. Further, by creating an industrial park out of a blighted area, the organization is combating community deterioration.

Section 4.03 of Rev. Proc. 2010-9, 2010-2 I.R.B. 258, provides that exempt status will be recognized in advance of operations if proposed operations can be described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed. A mere restatement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement. The organization must fully describe the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that its proposed activities will be exempt, the Service will generally issue a proposed adverse determination letter or ruling.

In The Church in Boston v. Commissioner, 71 T.C. 102 (1978), the Tax Court determined that an organization did not provide sufficient information for the IRS to determine whether grants to individuals were made in an objective and nondiscriminatory manner and whether the distribution of such grants was made in furtherance of an exempt purpose. The petitioner organization was unable to furnish any documented criteria that would demonstrate the selection process of a deserving recipient, the reason for specific amounts given, or the purpose of the grant.

In Share Network Foundation v. Commissioner, 78 T.C.M. (CCH) 6 (1999) the court provided that an organization has the burden of providing sufficient documentation or other substantive information regarding its activities and operations, which would establish entitlement to tax-exempt status.

In Solution Plus, Inc. v. Commissioner, 95 T.C.M. (CCH) 1097 (2008), the Tax Court provided that a charitable organization's programs must benefit the members of a recognized charitable class in a "nonselect manner."

ANALYSIS

You have asked us to recognize you as an organization described in § 501(c)(3). Based on the information you have provided, we find that you are not organized and operated exclusively for exempt purposes as described in § 501(c)(3).

Section 1.501(c)(3)-1(a)(1) states that to be described in § 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt. Section 1.501(c)(3)-1(b)(1)(i) states that an organization is organized exclusively for one or more exempt purposes only if its articles of organization limit the purposes of the organization to one or more exempt purposes and do not expressly empower the organization to engage, other than as an insubstantial part of its activities, in activities which are not in furtherance of one or more exempt purposes. Your Certificate of Incorporation states you provide struggling farmers with financial arrangements enabling them to avoid foreclosure after they've exhausted other means of assistance. However, assisting a class of persons not limited to a charitable class is not an exempt purpose. Your Certificate of Incorporation does not limit your purposes to exempt purposes.

In addition, Treas. Reg. § 1.501(c)(3)-1(b)(4) provides that an organization is not organized

exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. Your Certificate of Incorporation is silent regarding the disposition of your assets in the event of a dissolution, and therefore, does not meet the requirements of § 1.501(c)(3)-1(b)(4). Based on the foregoing, you are not organized exclusively for exempt purposes.

Under the standard described in § 4.03 of Rev. Proc. 2010-9, we will recognize your exempt status only if your operations are described in sufficient detail to permit a conclusion that you will meet the requirements of § 501(c)(3). You must fully describe your activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that its proposed activities will be exempt, the Service will generally issue a proposed adverse determination letter or ruling.

Your Form 1023 provides that B is your sole director, officer and employee. The Form 1023 also provided that you will not have a conflict of interest policy, nor will you document the terms of compensation arrangements. You will not base compensation on information about similarly situated organizations providing similar services. You failed to explain how you set reasonable compensation on your Form 1023. The Service requested more information about how you set the compensation for your sole director, officer and employee. You stated that you would cap the employee's salary to \$x annually, and that you believed the compensation to be fair as compared to the salaries paid to executives at large non-profits. The Service asked you to explain the how your determination of compensation relates to the actual work performed by the employee. You did not provide an answer. The Service also asked you to address any procedural safeguards to prevent your assets from being diverted for private purposes. You did not provide an answer. Your Form 1023 also provided that B owns intellectual property related to your programs. The Service requested you explain the terms of your agreements with B related to the use of B's intellectual property. You did not provide an answer. You have not fully described your standards, criteria, and procedures related to the nature of your expenditures to the extent necessary to demonstrate you further exempt purposes, and not private purposes.

Your primary activity is the provision of (i) interest-free loans to farmers and (ii) purchases of partial or full interests in farm property. B will make all determinations with respect to the loans. You have no procedures in place to ensure the loan amounts are being used for exempt purposes. While noncommercial lending is permitted by § 501(c)(3) organizations, it must be done in a manner that ensures it furthers an exempt purpose. See Rev. Rul. 56-304, *supra*, The Church in Boston v. Commissioner, 71 T.C. 102 (1978), and Solution Plus, Inc. v. Commissioner, 95 T.C.M. (CCH) 1097 (2008). You have not provided any documentation regarding policies or procedures aimed to ensure your loan recipients are members of a charitable class and were selected in an objective and nondiscriminatory manner. You have no documentation of policies or procedures to assure your loans do not benefit your officers and directors. You have no documentation of policies or procedures to ensure the loans are consistently used for the purposes which they were initiated. The information you provided regarding your loan procedures consisted of generalizations that did not enhance our understanding of your activities, and were not sufficient to determine that you are operated exclusively for exempt purposes. See Rev. Proc. 2010-9, *supra*, and Share Network Foundation v. Commissioner, 78 T.C.M. (CCH) 6 (1999).

Your Form 1023 states that you help poor and distressed farmers. The Service requested you describe any restrictions on which farmers are eligible for your loans. You responded that there are no restrictions on eligibility other than the farm being located in the U.S. or a U.S. territory.

You have no restrictions on the income, net worth, or emergency hardship of the farmers, or the geographic location of the farms. Without further restriction, farm ownership does not constitute a charitable class. See Solution Plus, Inc. v. Commissioner, 95 T.C.M. (CCH) 1097 (2008).

You are unlike the organization described in Rev. Rul. 74-587, *supra*, which limited its financial assistance to recipients that were otherwise unable to obtain funds from conventional commercial sources due to their location in depressed urban communities or the proprietor's membership in a minority or other disadvantaged group qualified for exemption. You are unlike the organization described in Rev. Rul. 76-419, *supra*, which provided financial incentive for industrial enterprises to locate in an economically depressed area. You have no restrictions on eligibility of your recipients other than the farm being located in the U.S. and its territories. Therefore, your activities do not necessarily promote exempt purposes.

CONCLUSION

Based on the information provided, you do not qualify for exemption as an organization described in § 501(c)(3) because you are not operated exclusively for one or more exempt purposes under § 501(c)(3). You must file federal income tax returns.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service

Attn:

1111 Constitution Ave, N.W.
Washington, DC 20224-0002

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Acting Director,
Exempt Organizations
Rulings and Agreements